

Date of Hearing: July 9, 2019

ASSEMBLY COMMITTEE ON JUDICIARY  
Mark Stone, Chair  
SB 472 (Caballero) – As Amended May 7, 2019

As Proposed to be Amended

**SENATE VOTE:** 35-0

**SUBJECT:** EARNED INCOME ACCESS SERVICE PROVIDERS

**KEY ISSUE:** SHOULD WORKERS BE ABLE TO USE THIRD-PARTY PROVIDERS TO ACCESS THEIR EARNED INCOME BEFORE THE DATE ON WHICH THEY WOULD ORDINARILY BE PAID, AND IF SO, WHAT SAFEGUARDS SHOULD APPROPRIATELY GOVERN THESE TRANSACTIONS?

**SYNOPSIS**

*Several companies currently offer services to provide Californians with an advance on their earnings in exchange for a fee. Some of these companies contract with employers to offer this service to their employees; these providers are repaid directly out of employees' paychecks. Others contract directly with workers; these providers are typically repaid from workers' bank accounts. All of these providers advertise themselves as less-expensive alternatives to high-interest payday and small-dollar lending.*

*This bill would enact a statutory framework to regulate these providers. Under this bill, providers would be required to register with, and be subject to examination by, the Department of Business Oversight; limited in the fees they could charge workers; prohibited from engaging in various forms of collections activity; restricted in their use of workers' personal information; and forced to maintain adequate liquidity to cover potential liabilities.*

*Stakeholders, including providers themselves, payroll processing companies, labor groups, consumer protection and advocacy organizations, privacy advocates, employment lawyers, and legal services organizations participated in a series of roundtable discussions and have provided significant input regarding the bill. The proposed amendments discussed in the analysis include much of this input and are explained and incorporated into the analysis. The bill, as proposed to be amended, is supported by its sponsor, PayActiv, and is opposed by the National Consumer Law Center.*

**SUMMARY:** Creates a regulatory framework for third-party companies to provide income advances to California workers in exchange for payments. Specifically, **this bill**, as proposed to be amended:

- 1) Would create a new division of the Financial Code entitled "Wage-Based and Work-Based Advances."
- 2) States that it is the intention of the Legislature to:
  - a) "Protect the interests of workers in this state who avail themselves of wage-based and work-based advances."

- b) “Provide for the safe, efficient, and orderly conduct of the business of providing wage-based and work-based advances.”
  - c) “Provide legal certainty to providers of wage-based and work-based advances by establishing a regulatory framework for their lawful conduct in this state.”
  - d) “Maintain public confidence in providers of wage-based and work-based advances.”
  - e) “Prohibit both employers and persons that hire independent contractors from directly profiting from workers’ use of wage-based and work-based advances.”
  - f) “Establish a registration and reporting system facilitated by the Commissioner of Business Oversight in order to provide the state with information about the number and size of businesses providing wage-based and work-based advances in California and about the evolving nature of their business models.”
- 3) Defines “worker” to mean a natural person who has earned wages or compensation in California, whether as an employee or as an independent contractor.
- 4) Defines “obligor” to mean either a) an employer, or b) a person other than an employer who is contractually obligated to pay a worker a sum of money on an hourly, project-based, piecework, or other basis for the worker’s labor or services. Excludes from the definition of “obligor” both the obligor’s customers and any third parties that have an obligation to pay the worker based on the worker’s status as the obligor’s agent.
- 5) Defines “wage-based advance” and “work-based advance” to mean funds advanced by a provider (as defined below) to a worker—if those funds are based on wages or compensation that the worker earned but not yet been paid—for work that the worker performed for or on behalf of an obligor.
- 6) Defines “provider” to mean a person engaged in the business of delivering wage-based or work-based advances.
- 7) Defines “payment” to mean the money or other consideration that a worker pays to a provider in exchange for providing the worker with a wage-based or work-based advance.
- 8) Requires a person to register with the Commissioner of Business Oversight before engaging in business as a provider.
- 9) Permits the Commissioner of Business Oversight to deny an application for registration as a provider if the applicant makes a false statement of material fact in the application or if the Commissioner has grounds to believe that approval is likely to result in harm to the public.
- 10) Permits a provider to offer a wage-based or work-based advance to a worker by contracting with an obligor (typically, an employer) so that the provider will advance funds to the worker and be repaid from the worker’s next paycheck. Such a contract is subject to the following conditions:
- a) An obligor cannot charge a worker for the costs of offering a wage-based or work-based advance, but can offer the provider’s optional services or service package to the worker

for a fee. The obligor cannot directly profit from the fee for these optional services, but must simply pass any fees through from worker to provider.

- b) An obligor cannot receive payments or other compensation from the provider related to workers' use of wage-based or work-based advances. Kickbacks from the provider to the obligor are prohibited.
- 11) Permits a provider to offer a wage-based or work-based advance to a worker by contracting directly with the worker for repayment. Such a contract is subject to the following conditions:
- a) A provider must notify a worker, at least two days before the date on which repayment is due, of the amount that is due and the date on which the provider will attempt to collect it from the worker. The notification cannot merely be provided through a mobile application which requires that the worker enter a password in order to access the notification.
  - b) A provider must make best efforts to ensure there are sufficient funds in the worker's deposit account before attempting to collect repayment.
  - c) A provider may make no more than three attempts at collecting repayment from the worker's deposit account, and may not charge the worker a fee for an unsuccessful transfer.
  - d) A provider may provide and charge a worker for separate and unrelated services, so long as the availability of wage-based and work-based advances is not conditioned on purchase of these services.
- 12) Permits obligors to share, with a worker's consent, information with a provider regarding the worker's earnings.
- 13) Specifies that a provider may require payment as a condition of providing a wage-based or work-based advance, or make such payment optional and in an amount determined by the worker (i.e., the so-called "tip" model).
- 14) Limits payments from a worker to a provider for wage-based or work-based advances to an average of \$15 per month for the first six months of the year, and again, for the second six months of the year. In other words, the most that a worker could be charged for advances is \$90 total between January and June, and again between July and December.
- 15) Prohibits a provider from requiring, under any circumstances, payments that total more than \$15 per month.
- 16) Prohibits providers from making more than three advances to a worker per week.
- 17) Prohibits providers from advancing more than 50 percent of the gross amount that an obligor owes to a worker at the date and time that the worker requests the advance; provides, however, that this limit can be exceeded twice during the first six months of the year, and twice again during the second six months of the year.

- 18) Prohibits the provider from charging a worker a different payment depending on which method of delivery is used to provide advances, but does permit an additional payment for expedited delivery if the amount of the payment is reasonable and proportional to the cost of expediting delivery.
- 19) Prohibits a provider from requiring a worker to open an account at a particular financial institution as a condition of receiving wage-based or work-based advances unless there is no fee charged to the worker or an obligor to open and maintain the account.
- 20) Provides that wage-based and work-based advances are to be provided only on a non-recourse basis, a term which, in this context, means all of the following:
  - a) A provider may not attempt to collect funds advanced to a worker, either directly or through a third party, or sell or transfer any right to collect to a third party.
  - b) A provider may not report a worker's repayment or failed repayment of a wage-based or work-based advance to any person other than the worker. Reports to consumer credit reporting agencies are explicitly prohibited.
  - c) A worker may not be held liable for a failed repayment of a wage-based or work-based advance if the obligor fails to meet its payroll obligation to the provider or worker.
- 21) Requires a provider to maintain a minimum net worth of \$250,000; a fidelity bond in the amount of \$250,000 or one-sixth of the total wage-based and work-based advances that it made in the last six months of the prior calendar year, whichever is greater; and an errors and omissions insurance policy in the amount of \$250,000 or one-sixth of the total wage-based and work-based advances that it made in the last six months of the prior calendar year, whichever is greater. Alternately, permits a provider to, instead of obtaining a bond and an insurance policy, place the appropriate amounts in an insured escrow account from which withdrawals may be made only by court order, order of the commissioner, or under Department of Business Oversight regulation.
- 22) Requires the provider to submit proof to the Commissioner of Business Oversight that it is meeting the requirements of 21).
- 23) Permits a worker to cancel participation in a wage-based or work-based advance program at any time without incurring a cancellation charge.
- 24) Requires providers to comply with applicable privacy laws, including the California Consumer Privacy Act of 2018, and forbids providers from selling, sharing, or otherwise disclosing a worker's personal information.
- 25) Provides the following remedies for violations of the laws governing wage-based and work-based advances:
  - a) Civil suit in a court of competent jurisdiction, with reasonable attorney's fees, costs, and expenses awarded to the prevailing plaintiff.
  - b) A claim against the bond, insurance policies, or accounts required under 21).
  - c) Civil penalties of \$2,000 per violation, payable to the Department of Business Oversight.

- 26) Requires providers, before providing a wage-based or work-based advance, to give workers a notice that includes information on how to cancel participation in the program, how to reach the provider, and how to file a complaint with the Department of Business Oversight. Requires that workers who access wage-based or work-based advances through an electronic application have access to an in-app link to this notice.
- 27) Requires providers to submit annual reports and financial statements to the Department of Business Oversight.
- 28) Provides to the Commissioner of Business Oversight examination authority and the power to order providers to either refrain from engaging in a specific business or activity, or to suspend business operations altogether.
- 29) Exempts delivery of wage-based and work-based advances from the Money Transmission Act, the California Financing Law, and the California Deferred Deposit Transaction Law, respectively codified at Divisions 1.2, 9, and 10 of the Financial Code.
- 30) Establishes a sunset date of January 1, 2023.

**EXISTING LAW** establishes the Department of Business Oversight and the office of the Commissioner of Business Oversight. (Financial Code Section 321.)

**FISCAL EFFECT:** As currently in print this bill is keyed non-fiscal.

**COMMENTS:** Several companies currently provide workers in California with advances on their paychecks and/or anticipated earnings in exchange for a fee. These companies operate under diverse business models, and it is unclear whether, and how, their operations fit within current California laws governing consumer finance and lending. This bill would therefore establish a statutory framework to begin regulation and oversight of this emerging industry.

**Background and justification for this bill.** It is by now well understood that many Americans live paycheck-to-paycheck and that emergencies such as unforeseen medical expenses can prove disastrous to their ability to make ends meet. The Federal Reserve's annual report on household well-being revealed that 39 percent of U.S. households do not have enough money to meet a \$400 emergency expense and that 17 percent of adults anticipated failing to make at least one bill payment during the month they were surveyed. (Van Dam, *Are Americans benefiting from the strong economy—aside from the rich? A Fed report raises questions*, Washington Post (May 23, 2019), available at <https://www.washingtonpost.com/us-policy/2019/05/23/americans-arent-ready-weather-sustained-downturn-new-report-shows/>.)

Faced with such shortfalls, many households turn to expensive sources of credit as a lifeline. An emerging set of businesses claim to provide an alternative, less-expensive source of funds compared to payday loans, by providing workers with early access to their incomes in exchange for a fee. According to the author:

For years, the Legislature has been trying to clamp down on predatory lending, and until recently there has not been a safer alternative to address the very real need of people accessing their money before payday. SB 472 seeks to create statutory clarity so Earned Income Access programs can continue to be a prudent and less costly alternative to payday lending. Earned Income Access is a socially responsible alternative for consumers that

simply allows them to access a portion of the wages that they have already earned before their next payday. These programs have been proven to reduce the demand for payday loans, and does so far more cheaply and with less risk for consumers.

There are essentially two models by which workers can gain early access to their earnings (termed “wage-based advances” and “work-based advances” under the bill).

Under the first model, the employer (termed the “obligor” under the bill)—typically a large corporation or other institution—contracts with a provider to make advances available to their workers. A worker can obtain an advance on their earnings from the provider, and on payday, the obligor repays the provider the amount advanced, plus a fee (termed a “payment” under the bill); the worker then receives the remainder of their paycheck. This model is commonly described by industry participants as a “business-to-business” model.

Under the second model, the obligor—typically a smaller firm or one that hires independent contractors—is not directly involved in the transaction. Rather, the worker provides satisfactory proof to the provider of the worker’s likely income and then obtains an advance on this amount. On the day that the provider expects the worker to be paid, the provider seeks repayment from the worker along with a payment for the advance, typically through a withdrawal from the worker’s bank account. This model is commonly described by industry participants as a “direct-to-consumer” model.

***Key issue: what is the appropriate level of regulation for these services?*** The fundamental issue presented by this bill is the appropriate level of regulation for companies that are providing Californians with wage-based and work-based advances. The following points are worth keeping in mind in deciding this question:

- A significant number of Californians don’t have enough money to deal with emergency expenses. Many of them have to resort to credit in order to make ends meet and avoid disaster.
- The Legislature must strike the proper balance between preventing foreseeable harms to consumers, and allowing new business models to be tried that provide these Californians with access to credit at prices that are more affordable than current options such as payday and small-dollar loans.
- Concerns regarding the risks of direct-to-consumer advances are warranted, but must be balanced against the fact that people who work for small businesses or as independent contractors regularly find themselves in need of emergency funds.
- The bill includes a broad set of consumer protections, described below, which seek to provide regulatory oversight, prohibit debt collection activity, protect consumer privacy, ensure adequate liquidity to deal with provider liabilities, and prevent collusion between providers and unethical employers.
- It remains to be seen whether this bill’s statutory framework will encourage the development of pro-consumer business models or lead to an exploitative race to the bottom, as has occurred in the payday lending space.

- No statutory framework is perfect, and loopholes may be exploited to the detriment of certain consumers. But this bill establishes a basic set of protections that can be strengthened, either by statute or rulemaking, in order to address consumer harms as they become apparent.
- Companies are already providing wage-based and work-based advances to Californians and more companies will join them.

In the absence of this bill, when confronted with allegations of consumer harm, regulators and the courts will be forced to try to shoehorn market actors into existing legal frameworks which may or may not prove adequate to addressing these abuses. For example, New York regulators recently subpoenaed documents from Earnin, one of the companies that has been involved in discussions around this bill, as part of an investigation into Earnin's potential violations of state usury laws. However, it is simply unclear whether Earnin is violating New York laws or not. (Dugan, *Cash-advance app Earnin gets subpoenaed by NY regulator: source*, New York Post (Mar. 28, 2019), available at <https://nypost.com/2019/03/28/cash-advance-app-earnin-gets-subpoenaed-by-ny-regulator-source/>.)

Alternately, California could take the approach of states like Arizona, Utah, and Wyoming, which are creating “regulatory sandbox” programs that allow so-called fintech (financial technology) companies to operate in “an environment free of onerous government restrictions.” (Kaye, *Utah's new regulatory sandbox* (Jun. 11, 2019) Ballard Spahr LLP, available at <https://www.consumerfinancemonitor.com/2019/06/11/utahs-new-regulatory-sandbox/>.) An unregulated or barely-regulated market is of course an optimal environment in which to allow potential predatory lenders to flourish.

Ultimately, this bill attempts to strike a sensible middle ground among the considerations outlined above, rather than leave providers operating without oversight.

***What protections does this measure provide for workers who obtain wage-based and work-based advances?*** As proposed to be amended, the bill would provide workers and obligors the following protections:

- *Regulatory oversight.* Providers of wage-based and work-based advances would be required to register with the Department of Business Oversight (DBO), which in turn would have examination authority over providers. DBO could issue orders addressing providers' violations of law, up to and including ordering providers to suspend their business operations altogether. DBO could obtain civil penalties of up to \$2,000 per violation against providers.
- *Right to cancel.* Workers could cancel their participation in a wage-based or work-based advance program at any time without charge.
- *Limits on fees.* Providers could not require workers to pay more than \$15 a month for advances; while workers could voluntarily pay more than this under the so-called “tip” model, workers' average monthly payments—as measured during the first six months of the year and again during the second six months of the year—could in no case exceed \$15 per month. Fees for expedited delivery of funds must be “reasonable and proportional” to the cost of expediting delivery.

- *Limits on advances.* Workers would be prohibited from obtaining more than 50 percent of their gross income in the form of an advance, though they could exceed this limit twice during the first six months of the year, and twice more during the second six months of the year. Workers could obtain no more than three advances per week.
- *Prohibitions on kickbacks.* Providers would be prohibited from compensating obligors in any way for their workers' use of wage-based or work-based advance services.
- *Bonding and insurance requirements.* In order to help ensure that providers found liable for legal violations can make plaintiffs whole, providers would be required to maintain both a bond and a separate errors and omissions insurance policy, each in the amount of its average monthly advance for the final six months of the previous calendar year. Providers would have to present proof of having met this requirement to DBO. (This requirement is particularly important given that certain providers have access to workers' bank accounts.)
- *Prohibitions on debt collection activity.* Other than attempting to obtain repayment of amounts advanced up to three times from a worker's bank account, providers could not engage in any debt collection activity, or sell or transfer the right to collect to a third party. Providers could not report a worker's repayment or failure to repay to any third party, including a consumer credit reporting agency. In order to reduce the risk of bank fees being assessed for insufficient funds, providers would be required to make best efforts to ensure there are sufficient funds in the worker's deposit account before attempting to collect repayment.
- *Privacy protections.* Providers would be subject to the CCPA, and would be barred from selling, sharing, or otherwise disclosing workers' personal information.
- *Private right of action with attorney's fees.* Providers could be sued in court, with the prevailing plaintiff obtaining its attorney's fees, costs, and expenses.

**Key issue: are wage-based and work-based advances loans?** One question that this bill presents is how the law is to categorize the obligations created by a wage-based or work-based advances.

Innumerable California Supreme Court opinions have made clear that the question of whether a transaction is a loan requires an examination of the substance of the underlying transaction, rather than its form. (See, e.g., *Milana v. Credit Discount Co.* (1945) 27 Cal. 2d 335, 340 ["The courts have been alert to pierce the veil of any plan designed to evade the usury law and in doing so to disregard the form and consider the substance."]; *Glair v. La Lanne-Paris Health Spa* (1974) 915, 925 ["[U]nder Truth-in-Lending we must look to the substance of the transaction and not allow mere form to dictate the result."]; *Boerner v. Colwell Co.* (1978) 21 Cal. 3d 37, 44 ["[T]he courts, alert to the resourcefulness of some lenders in fashioning transactions designed to evade the usury law, have looked to the substance rather than the form of such transactions in assessing their effect and validity, and in many cases have struck down as usurious arrangements bearing little facial resemblance to what is normally thought of as a 'loan' or a 'forbearance' of money."].)

Civil Code Section 1912 provides in pertinent part, "A loan of money is a contract by which one delivers a sum of money to another, and the latter agrees to return at a future time a sum



equivalent to that which he borrowed.” Both wage-based and work-based advances are based on a contractual agreement under which providers deliver a sum of money to a worker (based on the worker’s expected earnings) and the worker agrees to the return of an equivalent sum, either directly from the worker’s paycheck or from the worker’s bank account, to the provider. Consequently, it appears that wage-based and work-based advances would constitute loans under California law.

***Author’s amendment—preventing location-based advertising of the availability of an advance.***

While the author’s proposed amendments include significant privacy protections for workers, the bill would still fail to keep workers from being targeted for advances by providers when these workers are in situations where they could make purchases. It is certainly easy to imagine an app that sends an alert to the user which reads, for example, “Did you know you’re eligible for a \$100 advance?” when it detects that the user is in a department store or near a restaurant. (C.f., Kwet, *In Stores, Secret Surveillance Tracks Your Every Move*, N.Y. Times (Jun. 14, 2019) available at <https://www.nytimes.com/interactive/2019/06/14/opinion/bluetooth-wireless-tracking-privacy.html>.) There is a legitimate danger that income advance could turn into a service that plays on peoples’ desire for money at a time when they might be vulnerable to suggestion, instead of maintaining the service as an option for genuine emergencies. This is not to say that all app-based financial information from providers is necessarily harmful. Users would benefit from receiving information such as an alert that their bank account is getting low and their rent is due, and suggesting an advance on this basis.

In order to prevent location-based marketing, while continuing to allow the provision of genuinely-useful information, the author proposes the following amendment:

***Financial Code 60010. (d) A provider shall not utilize geolocation data, however derived, to present information to a worker regarding the availability of a wage-based or work-based advance, or to invite a worker to seek or obtain such information.***

This amendment is meant to correct for individuals’ tendency to value present consumption over future consumption, even if the former costs them more money, and to safeguard against attempts to manipulate this tendency. (See Hanson & Yosifon, *The Situational Character* (Nov. 2004) 93 Georgetown L. J. 1, 44-45 [“If you want \$100 today instead of \$200 in two years, but would prefer \$200 in eight years to \$100 in six, you are probably responding to the exterior situational salience of money today, in your pocket, ready to spend on all the items that likewise are comparatively available. Any of the other sums at future times are far less immediate...that we humans are unaware of this power renders us especially vulnerable to manipulation through external situation.”].)

***Next steps for this bill.*** Should this bill pass the Banking and Judiciary Committees, it will likely be amended further, in part to incorporate certain business models that are currently in operation but don’t fit cleanly within the bill, and in part to address concerns raised by the National Consumer Law Center in its letter of opposition. As an example of the latter, it may be appropriate to, for example, prohibit a payday lender that holds a license under the California Deferred Deposit Transaction Law from registering as a provider of wage-based and work-based advances. Discussions around this bill’s provisions are far from over, and if the bill is amended to diminish consumer protections, it is likely that this Committee will assert its power to re-hear the bill.

**REGISTERED SUPPORT / OPPOSITION:**

**Support**

PayActiv (sponsor)

**Opposition**

National Consumer Law Center

**Analysis Prepared by:** Jith Meganathan / JUD. / (916) 319-2334